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Federal Communications Commission
Washington, D.C. 20554

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OFFICE OF SECRETARY

COMMISSION

In the Matter of)
) CC Docket 96-45
Federal-State Board on)
Universal Service)

**COMMENTS OF THE ASSOCIATION
FOR LOCAL TELECOMMUNICATIONS SERVICES**

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CONTENTS

SUMMARY	i
I. ALTS' INTEREST IN THIS PROCEEDING	1
II. OVERVIEW	2
III. EXISTING SUPPORT MECHANISMS	4
IV. SUPPORT FOR RURAL, INSULAR AND HIGHT COST AREAS	9
A. Services for which Support Should be Included	9
B. Implementation - Calculation of the Subsidy	10
C. Eligibility for Support	12
V. SUPPORT FOR LOW-INCOME CONSUMERS	15
VI. CONTRIBUTIONS TO AND ADMINISTRATION OF SUPPORT MECHANISMS	16
A. Who Should Contribute	16
B. Assessment of Contribution	18
C. The Administrator	18
VII. MISCELLANEOUS	19
VIII. CONCLUSION	21

SUMMARY

The best way to encourage efficiency in the provision of telephone service and to satisfy the Commission's universal service goals is to encourage competition in all local markets. Competition will lower the cost of service, give consumers more choices and encourage the provision of better and different services. One important way that the Commission can encourage competitive entry into the local markets is to thoroughly review and completely revise the universal support mechanisms in a timely manner as contemplated in the Telecommunications Act of 1996.

In adopting changes to the universal service support mechanisms the Joint Board in making its recommendations, and the Commission in adopting new rules, need keep in mind only a few, relatively simple principles. The regulations adopted must:

- result in subsidies that can be carefully quantified, controlled, targeted, and explicitly linked to the provision of universal service for persons who might not otherwise be able to afford phone service.
- ensure that the distribution of any subsidy to a carrier be based upon the number of targeted subscribers a carrier serves and that all subsidies be "portable",
- require that all facilities-based local exchange providers be eligible to participate in any subsidies,
- require that funds be collected and disbursed in a competitively neutral, equitable and non-discriminatory manner by a neutral administrator,
- ensure that the calculation of any subsidy be delinked from ILEC costs or any "revenue requirement",
- require all providers of telecommunications services to contribute to subsidy funding, and
- be technology-neutral.

If the Commission can adopt new rules based upon these principles in a timely manner, it will have taken a major step towards accomplishing the goal of providing advanced telecommunications and information technologies to all Americans.

Before the

CC Docket 96-45

COMMENTS OF THE ASSOCIATION

The Association for Local Telecommunications Services

I. ALTS' INTEREST IN THIS PROCEEDING

ALTS is the non-profit national trade organization

As providers of local exchange services, the members of ALTS

Telecommunications Act of 1996 ("96 Act") be accomplished in a fair and competitively neutral basis.

II. OVERVIEW

The members of ALTS have consistently argued that the best way to encourage efficiency in the provision of telephone service and to satisfy the Commission's universal service goals is to encourage competition in all local markets. Free market forces are a far more efficient means of delivering products and services than is governmental regulation of monopoly providers. Rather than threaten universal service, as has been argued by some incumbent local exchange carriers ("ILECs"), competition in local markets will lower the cost of services, give consumers more choices, and encourage the provision of better and different services. After time, competition will reduce the need for universal service support mechanisms.

Although ILECs for years have raised concerns about the impact of competition upon universal service -- first in customer premises equipment, then in interexchange services and, now, in the local markets -- the Joint Board and the Commission should remember that in the same time period penetration rates and usage have increased while the costs to consumers of basic telephone service have become more affordable than at any time in the past.¹ The specter of damage to the goal of universal service has been used by ILECs to protect their monopoly revenue

¹ See FCC, Common Carrier Bureau, Trends in Telephone Service, Feb. 1995, Tables 2,5.

streams and forestall competitive provision of service.

We are encouraged by the recognition in the '96 Act and the Commission's Notice that existing support mechanisms have not been sufficiently targeted, have been nearly impossible to audit, and have not been adequately linked to the provision of service for those who might not otherwise be connected to the public switched network.² Consistent with the '96 Act the following principles should guide the Joint Board and the Commission in adopting regulations to implement Section 254. The regulations must:

- result in subsidies that can be carefully quantified, controlled, targeted, and explicitly linked to the provision of universal service for persons who might not otherwise be able to afford phone service.
- ensure that the distribution of any subsidy to a carrier be based upon the number of targeted subscribers a carrier serves and that all subsidies be "portable",
- require that all facilities-based local exchange providers be eligible to participate in any subsidies,
- require that funds be collected and disbursed in a competitively neutral, equitable and non-discriminatory

² As one set of commentators described it, the existing universal service scheme has "evolved into a rat's nest of implicit subsidies and accounting sleights-of-hand utterly unsuited to a competitive marketplace." Huber, P., Kellogg, M., Thorne, J., The Telecommunications Act of 1996 (1996).

manner by a neutral administrator,

- ensure that the calculation of any subsidy be delinked from ILEC costs or any "revenue requirement",
- require all providers of telecommunications services to contribute to subsidy funding, and
- be technology-neutral.

In order to ensure that the above principles are followed and that, in fact, there is a direct connection between any subsidy and subscription to telecommunications services, it is important that the Commission also adopt specific, quantifiable and observable means of tracking the subsidies and their effects on residential subscription rates.

If the Commission is successful in adopting universal service support mechanisms that accomplish the goals listed above, it will encourage the provision of new, varied and affordable service to all Americans. If, on the other hand, the Commission adopts a system that is not sufficiently targeted and limited, it will create a category of consumers, primarily in "high cost" areas, that will never see the benefits of competitive provision of service and the information age.

III. EXISTING SUPPORT MECHANISMS

The '96 Act requires that any federal universal service support provided to eligible carriers be "explicit". Although there is no definition of "explicit" contained in the '96 Act, Congress was seeking to ensure that all subsidies be

specifically identified and targeted as universal service subsidies and are implemented in a manner that ensures that the connection between the subsidy and universal service goals can be easily monitored.³ In addition, any support mechanism must be available to all eligible carriers and must be administered in a non-discriminatory manner. The '96 Act contemplates that any support mechanism adopted should be limited to the amount necessary to accomplish the universal service goals for which it is intended.⁴

The validity of a number of current subsidies is brought into question by the '96 Act. These include the the Universal Service Fund ("USF"), Common Carrier Line Charge (the "CCL"), Long Term Support ("LTS"), and Dial Equipment Minutes ("DEM") weighting. The Notice raises the question whether any of these mechanisms can be retained as they are now structured.

The Universal Service Fund provides assistance to LECs with purportedly higher than average local loop costs. Generally, the Commission allows LECs to allocate 25 percent of their local loop costs to the interstate jurisdiction. Under the USF, however, the Commission allows LECs with reported local loop costs 115 percent above the nationwide average to allocate an additional

³ See also Section 254(b)(5) which requires that all subsidies be specific and predictable.

⁴ As the Commission is aware there is strong evidence that Universal Service Fund subsidies have increased substantially with no concrete proof that the increase has had any effect whatsoever on universal service goals. This must be curtailed.

amount of the local loop cost to the interstate jurisdiction. The USF is funded through a tariffed interstate charge paid by interexchange carriers (except that small carriers are exempt).

The CCL charge paid by the IXC's was adopted to provide ILEC recovery of the portion of the loop costs allocated to the interstate jurisdiction that is not recovered through the subscriber line charge (SLC) which is capped at \$3.50 per month per residential line. In theory, at least, the LTS is a mechanism for geographic averaging of the CCL. ILECs operating in lower cost areas contribute to the LTS fund, administered by the National Exchange Carrier Association (NECA). NECA provides higher-costs ILECs who are members of the NECA pool with sufficient support to enable them to charge IXCs a nationwide average CCL interstate access rate rather than the higher rate that might be charged based on their reported higher costs.

Finally, the DEM weighting factor allows ILECs with fewer than 50,000 access lines to allocate to the interstate jurisdiction a greater proportion of their local switching cost than larger ILECs may allocate. Thus, the interexchange carriers who pay switched access charges to the smaller ILECs (and the interexchange carriers' customers) fund the DEM weighting subsidy.

None of the existing support mechanisms described above should be allowed to continue as presently constituted. First, because they are not available to competitive providers, they are discriminatory, and violate the pro-competitive stance of the '96

Act. Second, they are not targeted or limited specifically to consumers that would otherwise be unable to obtain affordable local service. Third, they provide no incentive for the LECs to invest efficiently and result, instead, in the preservation of ILEC revenues regardless of efficiencies in the operations of the ILEC. In a competitive environment none of these programs can be justified.

The USF, as it has developed, does not withstand scrutiny under the '96 Act. It is not available to competitive carriers and thus serves as a barrier to entry by competitive local providers. Even in areas where competitors costs may be lower than the ILEC costs, competitors may decide not to commence provision of service due to the ILEC's ability to price services below cost. The USF also is not well targeted; it allows any ILEC with reported loop costs 115% above the nationwide average to allocate additional loop costs to the interstate jurisdiction regardless of any other factors that might influence the total cost of service. Finally, the fund has grown at a rapid rate with no demonstration that it has affected the number of persons connected to the public switched network.

The CCL ostensibly recoups non-traffic sensitive loop costs allocated to the interstate jurisdiction that are not recovered through the subscriber line charge. While the CCL raises a number of questions as to whether it can be justified under the '96 Act since it is not targeted nor competitively neutral, the Commission must first look at the underlying allocation of costs

and the jurisdictional separation of those costs. There is evidence that the total costs allocated, and, specifically, the costs allocated to the interstate jurisdiction, are simply much higher than they reasonably should be. While the Commission should be reconsidering the method of recouping these costs, it should, in the first instance, make sure that it is considering the correct amount of costs. It may be that the CCL can be eliminated in a relatively short time with no real affect on end-user prices. Futhermore, the advent of competition in interstate access markets effectively precludes any long-term reliance on the CCL mechanisms.

DEM weighting factor is available to all smaller ILECs regardless of the actual switching costs of that ILEC. While it previously may have been true that, in general and on average, the costs of switching for smaller ILECs was greater than the costs of switching for the larger ILECs, new technologies have narrowed whatever cost differences there may have been. In addition, the DEM weighting factor was initially introduced at least in part to aid smaller companies transition from analog to digital switches. This goal has been accomplished. The weighting factor is an out-dated, inefficient, discriminatory, and poorly targeted method of supporting costs that are not even proven to be in need of universal support.

The LTS suffers from some of the same problems from which weighted DEMS suffers. It is not well targeted nor designed to encourage efficient investment by LECs. In addition, it may

discourage efficient entry in markets served by LEC recipients of LTS.

IV. SUPPORT FOR RURAL, INSULAR AND HIGH COST AREAS

A. Services for which Support Should be Included

The NPRM seeks comment on the services that should be included among the core services receiving universal support. Tentatively, the Commission concluded that such services ought to include "(1) voice grade access to the public switched network with the ability to place and receive calls; (2) touch-tone; (3) single party service; (4) access to emergency services (911); and (5) access to operator services."

As competitive exchange service providers, the members of ALTS believe that the Commission's proposal is a good start. Clearly, the Commission has attempted to satisfy the congressional criteria while keeping in mind that too narrow a definition would not accomplish the universal service goals, while too broad a definition would cause the level of subsidy required to be unnecessarily inflated. At the same time, two other functions satisfy the congressional criteria for inclusion in the services for which support is available. These are access to directory assistance and directory listing.⁵

⁵ These functions appear to satisfy each of the four criteria enumerated by Congress. Directory assistance and listing is essential to education and public health and safety, is subscribed to by a substantial majority of residential customers, is deployed in public telecommunications networks and is consistent with the public interest, convenience and necessity. Without these two functions, use of the public switched network may be severely curtailed and the benefits of adding persons to the network would be lessened.

The Commission sought comment on whether the services proposed (and any additional services) would serve as a barrier to entry by new competitors or favor one technology over another. The services considered will not serve as a barrier to entry so long as the other principles enunciated in the '96 Act are implemented in a reasonable, timely and competitively neutral manner. For example, the provision of emergency services will not be a barrier to entry if the ILECs satisfy the section 251 interconnection and unbundling requirements in a reasonable manner. On the other hand, any of the services mentioned above could serve as a barrier to entry if the unbundling and interconnection requirements of Section 251(c) are not satisfied. In addition, inclusion of any of the services proposed above could result in a barrier to entry if the distribution of any support mechanism under Section 254 were not accomplished in a competitively neutral manner. Subsidies must be available to all eligible carriers.

B. Implementation - Calculation of the Subsidy

The Commission has identified principles under which it should calculate and collect any subsidy. The Commission stated:

"The method we ultimately adopt should be as simple to administer as possible, technology-neutral, and designed to identify the minimum subsidy required to achieve the statutory goal[s] It should be equitable and non-discriminatory in the burden that it imposes upon contributors, and its distribution procedures should be direct, explicit and specific."⁶

⁶ Notice at para. 27. In addition, of course, as the Commission recognized, the distribution of the subsidy must be competitively neutral.

We agree. At the same time, an additional principle should be added as follows: determination of the amount of support must be separated from ILEC costs or any supposed "revenue requirement." One of the biggest problems with the current universal support mechanisms is that determinations of whether support is warranted has been based solely on the ILECs' reported costs. This has encouraged inefficient operations, overbuilding and the overvaluation of plant. In order to cure these problems the determination of the amount of the required subsidy must be separated from LEC costs and must be based, instead, on an analysis of physical and other characteristics of the particular area. This analysis should reflect the cost of service that would be provided by an efficient competitor using appropriate technology. This will help ensure that the subsidy is the minimum amount required to achieve the universal service goals.

The Notice seeks comment on four methods for implementing universal service support for rural and high cost areas. The first is continued use of the Commission's jurisdictional separations rules. As noted above, this alternative is clearly unacceptable as it is not competitively neutral, provides no incentive for a LEC to control or reduce costs, and is not explicit. A second alternative is a proxy model proposed by Pacific Telesis that incorporates customer specific location data.

A third proposal is a model submitted to the Commission in Docket 80-286 by MCI Communications Inc., NYNEX Corporations, Sprint/United Management Co., and US West, Inc. ["Joint Parties Model"]. These carriers have developed a Benchmark Costing Model

for calculating an assumed level of expense for the provision of service by a wireline carrier in every census block group in the United States (with the exception of Alaska and the territories). The final proposal is a competitive bidding process whereby competing carriers would bid to set the level of assistance per line that any carrier serving a specified area would receive, with the low bid setting the amount any authorized carrier would receive. The Commission recognized that there may be insufficient competition at this time to ensure that a bidding process would work in all situations.

Either the Joint Parties Model or the competitive bidding process, or a combination of the two, would be an improvement over the present system. The total amount of subsidies should drop when no longer based solely upon LEC-provided data. In addition, either proposal would encourage efficient provision of service.⁷ A bidding process would help to identify those areas that, despite higher than average costs, have sufficient revenue sources to support provision of service without universal service support.

C. Eligibility for Support

The '96 Act makes clear that universal service support

⁷ The proxy model submitted by Pacific Telesis includes insufficient information and raises too many questions for ALTS to determine whether it would be an improvement over the current system. One problem with the proxy model envisioned by the Joint Parties is that it is not technology neutral and only addresses service provided by wireline carriers. There appears to be no reason why the model could not be altered to also consider non-wireline provision of service where that would be economical. Another potential problem with the proxy model is there is clearly a possibility of protracted disputes relating to the appropriate factors to be considered in individual areas.

should be available to competitive providers of local exchange services. This is one of the most important changes to the current system and should help ensure that whatever support mechanism is ultimately adopted will be targeted to universal service and will be the minimum amount necessary to accomplish the stated goal of ensuring that "quality services . . . be available at just, reasonable and affordable rates" to all the people of the United States.⁸

The Commission has sought comment on a means to ensure that all eligible carriers -- and no ineligible carriers -- receive the appropriate amount of universal service. ALTS believes that the Commission's concerns about ineligible carriers receiving support is probably unfounded. A carrier would not receive support unless it was found to be "eligible" by the state commission under Section 214(e)(2), and a carrier will become ineligible if it fails to offer services supported by the universal service support mechanisms.⁹

With respect to the issue of how to ensure that eligible carriers receive the appropriate amount of support, ALTS respectfully suggests that the best means of ensuring nondiscriminatory access to and calculation of support amounts is

⁸ Section 254(b)(1). Without the ability to participate in subsidies, new competitors have had little incentive to serve "high cost" areas or low income consumers since they have faced a serious cost disadvantage vis-a-vis the ILECs.

⁹ Under Section 214(e) the state must find competitive carriers to be eligible for universal service support in non-rural areas and may find them eligible in rural areas. The FCC may want to monitor the State actions in this regard to ensure that rural areas get the benefits of competitive entry in those markets.

to target support to the end-users who would not otherwise be able to afford service in a competitive market. Today, subsidies to high cost areas flow generally to telephone companies without any identifiable connection between the monies received and the customers in need of assistance. In the future, universal service support to these areas should be directly tied to end-users. The telephone user would direct, by making a carrier selection, to which carrier the universal support should flow. All universal service support monies should have a direct correlation to an end-user for whom service is provided. If a customer changes carriers, the subsidy would follow to the new carrier.

Finally, in order to ensure that carriers receive the appropriate amount of support, it is vital that the Commission ensure that the administrator picked by the Commission be a neutral administrator with no ties to any carrier.

The Commission also has asked how it can be assured that any support is used only for the purpose for which it is intended. There probably is no absolute guarantee that the support is actually and fully used for the purpose for which it is intended. Probably the most important thing that the Commission can do at this time to attempt to ensure that the support is used for the purposes for which it is intended is to make the support mechanisms explicit rather than implicit. In addition, of course, to the extent the amount of support is set at an appropriate level, there will be far less ability to use any support for inappropriate purposes.

The Commission should not require detailed accounting and

reporting requirements. This would be overly burdensome for the new competitive service providers (and probably ineffectual with respect to the incumbent local exchange carriers).¹⁰

V. SUPPORT FOR LOW-INCOME CONSUMERS

Today, there are two support mechanisms adopted specifically to aid low income subscribers, the Lifeline Assistance Program ("LAP") and Link Up America programs. LAP, which is administered by the states, reduces the monthly payment for eligible persons by the amount of the SLC, or in some cases double the SLC. The Link Up program helps to pay some of the initial installation charges so that persons who otherwise could not afford the initial fees can receive service.

Generally speaking, LAP and the Link Up America programs have served their purpose well. The Commission should clarify its rules, however, to state that low-income customers should be permitted to take service from any local carrier and continue to qualify for assistance. As with all support mechanisms for high cost areas, all low-income support mechanisms should be made "portable" and available to whichever carrier the customer designates. All such support mechanisms should, therefore, be stated in terms of specific dollar amounts, rather than in terms of a percentage discount.

Finally we note that the Link Up program is currently only

¹⁰ Likewise with respect to the Commission's obligation of ensuring the availability of "quality" services, the Commission should not adopt any new reporting requirements relating to technical performance levels.

available for connection to wireline service. In keeping with the principle that all subsidies should be technology neutral, the Commission should broaden Link Up eligibility to include non-wireline services at least in those areas where service can more economically be provided with other technologies.

VI. CONTRIBUTIONS TO AND ADMINISTRATION OF SUPPORT MECHANISMS

A. Who should Contribute

The Commission seeks comment on "whether passage of the 1996 Act should change existing assumptions about the sources of universal service support." The '96 Act states that all "providers of telecommunications services" should make an "equitable and nondiscriminatory contribution to the preservation and advancement of universal service". The '96 Act further provides that all carriers that provide interstate telecommunications services shall contribute to the mechanisms established by the Commission and that carriers providing intrastate telecommunications shall contribute in the manner adopted by the states. Thus, the '96 Act clearly contemplates two separate mechanisms supporting universal service - a federal mechanism and state mechanisms.

It is clear that Congress sought a reconsideration of all aspects of traditional universal subsidies and mechanisms and this includes the sources of support.¹¹ Traditionally, the

¹¹ See Conference Report discussion relating to section 254: "The conferees intend that, in making its recommendations to the Commission, the Joint Board will thoroughly review the existing system of Federal universal service support."

burden of most universal support funding has been borne by interexchange carriers and their customers through the access charges. Numerous carriers and other non-carrier providers of service have not been required to contribute to universal service funding. As noted above, one of the primary goals enunciated in the '96 Act is that "all providers of telecommunications services" should make contributions to the preservation and advancement of universal service. Thus, it is clear that Congress intended to broaden the universe of contributors to universal service. In doing this, the Commission should ensure that any rules it adopts in this regard are technologically neutral and treat all providers of similar services in a similar manner. This clearly may include non-carrier providers of telecommunications services and should, at the very least include local exchange companies (both incumbent and competitive), interexchange carriers, cellular providers, PCS carriers, and pay telephone providers.

Finally, the Commission seeks comment on which carriers might equitably be exempted from contributing to universal service. The Act provides that the Commission may exempt a carrier or class of carriers if the carrier's telecommunications activities are limited to such an extent that the level of such carrier's contribution to the preservation and advancement of universal service would be de minimus. The legislative history makes clear that Congress sought to exempt those carriers for whom "the administrative cost of collecting contributions . . . would exceed the contribution that carrier would otherwise have to make under the formula for contributions selected by the

Commission."

B. Assessment of Contribution

With respect to the method of assessing the contribution to be paid by carriers, the Commission suggests three alternatives: contributions based on gross revenues, contributions based on revenues net of payments to other carriers and contributions based on per-line or per-minute charges. The appropriate assessment is on the revenues net of payments to other carriers. This method is easy to administer and competitively and technologically neutral. Contributions based on gross revenues would result in double payments whenever a provider purchases access or network elements from a carrier. The per-line or per-minute calculation is more difficult to administer than revenues net of payments to other carriers.

C. The Administrator

As noted above, one of the most important factors in ensuring that the support mechanisms are administered in a competitively neutral and non-discriminatory manner is to ensure that the administrator of the support mechanisms be completely neutral and have no affiliation with any carrier.¹² We recognize that the National Exchange Carrier Association (NECA) has experience in administering some of the support payments that have heretofore been part of Universal Service. However, NECA

¹² The Commission recognized this when it stated that it seeks comment on the "best approach to administer the universal service mechanisms fairly, consistently and efficiently" and that it wanted an administrator that could administer funds in a "competitively neutral manner."

also functions as a representative of the ILEC industry. Its experience is entirely tied to the administration of funds to ILECs, not to competitive carriers. Thus, it does not appear that NECA has any particular experience that would aid it in administering a program under a competitive environment or would be sufficiently neutral in administering the support payments.

One alternative would be to have the states or the Commission administer the funds. This is not a viable option as most states and certainly the Commission have neither the experience or the staff to fully implement such a program. Rather than act as administrators, the states and the Commission should be arbitrators when the need arises.

The Commission should put out an RFP seeking an entity to administer the Universal Service Fund. The Commission should seek an entity that has experience as a clearinghouse. The Commission should not consider any entity that has close ties either through ownership, directorship or any other means with a particular segment of the telecommunications industry. There are a number of accounting, banking and other firms that have the experience and managerial capabilities to administer the support mechanisms.

VII. MISCELLANEOUS

The NPRM seeks comment on a number of general issues. First it asks how the Commission should satisfy its statutory obligation to ensure that "[Q]uality services should be available" to consumers. The Commission asked specifically whether it would be useful to collect and publish certain basic information regarding technical performance levels of carriers

subject to its jurisdiction.¹³ This appears to be unnecessary. The Commission stated that providing consumers with easy access to publicly available data on the performance level of various carriers may induce carriers to compete for customers on the basis of service quality and, presumably spur greater reliability and quality in the provision of service. However, the submission of reports to a Federal agency is hardly likely to increase the consumer's awareness of service quality or spur competitors to provide higher quality series. Normal market forces will provide all the incentive necessary to the provision of high quality service.

In addition, the submission of such information to Commission could serve as a barrier to entry for small service providers. One of the major thrusts of the '96 Act is to lessen barriers to entry caused either by market, or regulatory forces. Initiation of a new reporting requirement would violate many of the pro-competitive, deregulatory thrusts of the '96 Act.

Finally, the members of ALTS encourage the Joint Board and the Commission to implement the changes envisioned by the Act in a timely manner. The Act requires the Joint Board to recommend a "specific timetable" for the completion of such recommendations. It would be inconsistent with the pro-competitive thrust of the Act if the implementation of any universal service reforms were not accomplished in a timely fashion. Although there may be a need to phase in some reforms, there are many others, such as

¹³ Some of this information is currently collected from ILECs on the Automated Reporting and Management Information System (ARMIS).

portability of universal service support, that could be accomplished soon after the enactment of the rules. The Commission should ensure that the benefits of competitive provision of service to all Americans is encouraged and implementation of universal service reform in a timely manner will further that goal.

VIII. CONCLUSION

The Joint Board and the Commission have a difficult task ahead of them. The '96 Act requires a completely new look at all universal service support mechanisms and Congress has not given the Board or the Commission much time to accomplish this task. Nonetheless, if the Board and the Commission do not waiver from, and base their decisions on, the basic principles of nondiscrimination, competitive neutrality, equitable assessment and distribution of funds and a specific and quantifiable means of tracking all subsidies, ultimately the Joint Board and the

Commission will have fulfilled their statutory duty and furthered the pro-competitive purposes of the '96 Act.

Respectfully submitted,

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